



FAIR TRADE CENTER

SUSTAINABLE PURCHASING PRACTICES

**A SUMMARY OF A STUDY ON HOW PURCHASING PRACTICES
CAN BE ADJUSTED AND DEVELOPED TO IMPROVE SUSTAINABILITY**

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Published in March 2013

This publication is a summary version of Fair Trade Center's report "Hållbara inköpsmetoder – En studie av hur inköpsmetoder kan utvecklas och påverkas för att nå ökad hållbarhet". The report is based on in-depth interviews with eight Swedish companies: IKEA, H&M, Åhléns, Clas Ohlson, SCA, Volvo Group, Lindex and Filippa K. Additional material has come from corporate case studies of the aforementioned companies and from academics, consultants and human rights organisations.

The purpose of the report is to inspire further debate about sustainable purchasing practices for companies and other interested parties. The report should not be seen as an attempt to assess the companies' sustainability work in general. Fair Trade Center has based its study on the companies' own descriptions of the different ways in which they have developed their purchasing processes to make them more sustainable. There have been no independent field studies to verify the companies' sustainability work in practice.

This publication has been produced with the financial assistance of the Swedish International Development Cooperation Agency (SIDA). The content of this publication is the sole responsibility of Fair Trade Center and can in no way be taken to reflect the views of SIDA.

Layout: Lina Garemark

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What are sustainable purchasing practices?

Swedish companies have been increasingly choosing to move their production to low-wage countries, bringing new challenges to purchasing processes. Price focus, distances, language barriers and cultural differences have all made purchasing more complex. Meanwhile lead times have reduced as many markets have become more sensitive to trends. Time and price pressure have meant that factory floor workers are required to do unreasonable overtime and their wages are often not enough for them to live on.

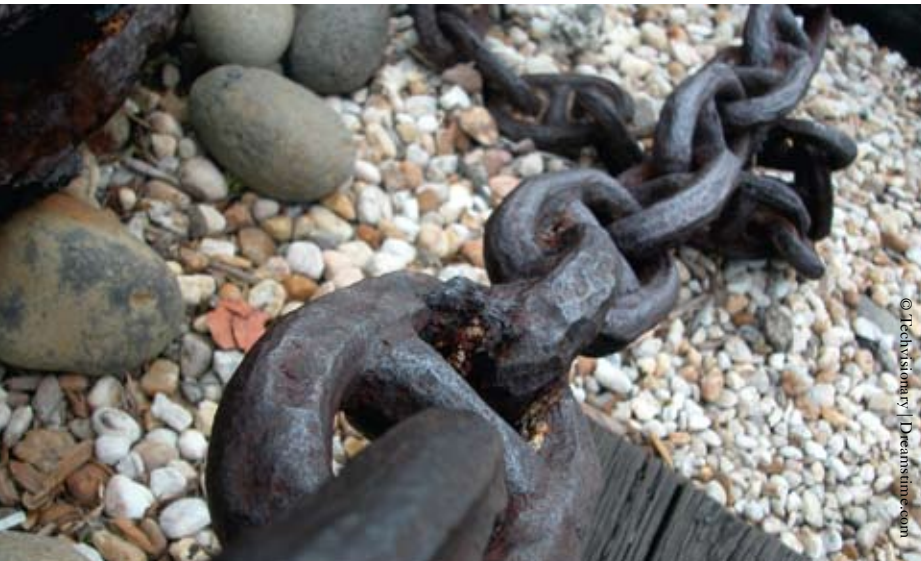
In other words there is a great need to develop sustainable purchasing practices. Fair Trade Center defines sustainable purchasing as follows:

SUSTAINABLE PURCHASING IS A PROCESS IN WHICH AN ORGANISATION BUYS ASSETS, PRODUCTS OR SERVICES, TAKING FACTORS SUCH AS FINANCIAL VALUE AND THE ENVIRONMENTAL AND SOCIAL IMPACT OF THE PURCHASE INTO CONSIDERATION.

There is much room for improvement when it comes to purchasing practices and it is not possible to talk about ideal solutions or “best practise”, since in many areas the methods used do not fulfil their aims. However, Fair Trade Center does consider it worth discussing steps that have been taken in the right direction. It therefore wants to highlight a few good examples of sustainable purchasing practices and

ways in which companies can make existing purchasing practices more sustainable. Questions concerning sustainable purchasing practices are relatively new and sufficiently complex for Fair Trade Center to acknowledge that the report probably does not cover all the relevant aspects. It therefore welcomes any attempts to further develop the debate and provide new perspectives.

The integration of a verification system for corporate responsibility, increased cooperation with suppliers, and the development and change of traditional purchasing practices, are examples of how purchasing practices can be made more sustainable. These will be explored in further detail in this publication.



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Looking beyond codes of conduct

Nowadays, 60-70 % of a company's product manufacturing costs are made up of invoices from suppliers of products or services. At the same time the market has become increasingly sensitive to trends. In an attempt to reduce costs and improve efficiency it has become increasingly common to move production to low-wage countries. With this in mind, companies have looked for the fastest delivery times at the lowest prices on the global market. This new strategy has had a marked impact on purchasing processes and it has involved considerable changes in many purchasing departments.

Purchasing has gone from being quite an anonymous part of a company's organisation to having a much more strategic role. Purchasing processes and supply chain management are more important to

companies than ever before. This is not only because of competition and pricing, but also due to the fact that ethical arguments have become particularly important to purchasing departments in recent years.

Moving production to low-wage countries also involved new risks. Problems of child labour, forced labour, unreasonable working conditions with excessive overtime and low wages became great challenges – and in many areas the problems persist. The systematic discrimination of workers, as well as threats and redundancies for wanting to join free trade unions remains a serious problem. Violations of human rights in the corporate supply chain sparked a debate, often driven by human rights organisations and trade unions,

about corporate responsibility and how companies could be held responsible for working conditions in their production chain, even if production was managed externally. It soon became apparent that companies lost out, both from financial and marketing perspectives, by appearing to act irresponsibly with respect to working conditions in the countries where their products were being manufactured. It was thus a development that presented a risk that needed to be managed. Transparency towards suppliers became increasingly important in this regard and contracts with suppliers, often in the form of codes of conduct, became increasingly common. From 1996 to 2009 the usage of well-functioning codes of conduct became standard practice for more and more companies. Indeed there has been a tremendous development in this area during the last 15 years. In line with this development, the United Nations (UN) presented its Guiding Principles on Business and Human Rights in 2011 to clarify the responsibility companies have towards their suppliers. This has also had repercussions on other international organisations. Nowadays, it is a matter of course that companies bear a social responsibility for their production processes. However, there is also a

great deal of debate about how far such responsibility should extend.

In recent years there has been a tendency for the focus to move beyond codes of conduct to ensuring that demands are actually met. Since codes of conduct have become more important, and companies are increasingly choosing to change and develop their supplier relationships, there is an increased need for formal procedures. Companies nowadays train and employ staff with specialist knowledge on corporate social responsibility (CSR), and they are even investing in tools and methods to improve the integration of sustainability questions within their organisations, not least with respect to purchasing processes. The way that companies view their suppliers has also undergone considerable change in a relatively short period of time. Before, suppliers were seen as an opposing party, and the only role of the buyer was to minimise costs. In some respects the traditional methods have developed, and planning and cost estimation tools can indeed be used to include sustainability factors, as noted by a number of companies. However, in general it seems that there is quite a way to go when it comes to widespread usage of sustainable purchasing practices.

Integration of verification systems for corporate responsibility

Social audits create a higher degree of accountability in areas that can be measured. They can clarify problems and challenges in concrete terms, providing incentives to share information about the change process, internally as well as externally. Since the quality of social audits is dependent on the time, resources and competence the buyer chooses to invest, there is a considerable risk that the results may be superficial or even misleading. However, it has also transpired that codes of conduct and social audits have difficulties assessing areas in which measurability is more limited or complex. Discrimination and trade union organisation are two such areas. For the method to have any effect, there must be additional follow-ups, such as action plans and time schedules for corrective

measures. It has become evident that many actors – interested parties as well as companies – do not regard social audits per se as being enough. Other methods are needed to complement the snapshot that the social audits can, at best, provide. Several companies regard the use and inclusion of workers and/or workers' representatives to be a complementary method to the social audits. It also helps to ensure that co-determination routines are established and that trade union or workers' representatives can influence the change process. Different methods of managing complaints mechanisms for factory workers can also be used to complement the social audits.

It is important for questions concerning sustainability to be firmly entrenched at management level, and for

the integration of questions concerning sustainability and purchasing processes to increase awareness and facilitate more sustainable purchasing practices. There are many different ways of integrating sustainability and purchasing processes. H&M has developed extensive internet-based solutions and databases, and it combines these with a high degree of accountability in its social audits. It then communicates the results to other parts of the organisation, as well as to external contacts, including suppliers. H&M states that it also works on long-term change processes in cooperation with its suppliers. The furniture giant IKEA

has chosen to place the responsibility for codes of conduct and follow-ups with its purchasing department, which it says better integrates sustainability and purchasing, and provides clarity vis-à-vis its suppliers. A third method for improving integration can be to complement sustainability work by making use of external audits and then incorporating the external system into one's own purchasing processes. The Åhléns department store chain has used this method since it signed up to the BSCI's Code of Conduct. It has integrated the auditing system into its internal tools to compare suppliers.

1. The Business Social Compliance Initiative (BSCI) is a business-driven initiative providing social audits and a verification system.

Increased focus on cooperation with suppliers

It is extremely important to build long-term relationships with suppliers to be able to pursue sustainable purchasing. Buyer companies can have different types of relationships with their suppliers. Traditionally there are two extremes when it comes supplier relationships in the purchasing sector: long-term partner relationships and “arms-length relationships”. To have a partner relationship with a supplier means that the company chooses to engage in long-term cooperation, rather like a partnership, and the buyer company invests in training and involves the supplier in product development. Having an “arms-length relationship” means that the company is not planning for long-term cooperation with a particular supplier. Instead, the purpose is to encourage suppliers to compete and

to quickly be able to accept a better offer from another supplier. The companies featured in the report have all adopted a minimum level of sustainability with their suppliers.

To get suppliers to strive towards the same sustainability goals as the buyer company, different factors need to be weighed in. The report shows that scoring systems can be a way to make targets more tangible, and to reward suppliers for their sustainability efforts. The hardware store chain Clas Ohlson has developed a scoring system in which the results from the social audits are taken into account in the overall evaluation of a supplier. The company has developed a systematic way of rewarding suppliers for showing ambition in the social audit. H&M has also developed a tool for rating suppliers,



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in which the suppliers' performance in the social audit weighs in heavily when the company places new orders.

"We want to take this a step further, so that suppliers are actually driven by the fact that they feel that they will be rewarded for making improvements and for being sustainable suppliers. The system means that the entire production chain works to reward and place more orders with those suppliers who achieve a high score in our social audits. So suppliers notice that they get more orders if they were work with these questions progressively."

Karin Rehnberg, Social Sustainability
Business Controller, H&M

Proximity to supplier

Procurement from low-wage countries has made communication more complicated. Communication with suppliers is important, both for planning production processes and costing issues, as well as for gaining an understanding of their sustainability work. Factors such as geographical distance, cultural differences and language barriers challenge communication. In this regard several companies confirm that geographical proximity to suppliers and long-term cooperation creates better premises for improved communication and deeper understanding of a supplier's situation. Two of the eight companies have chosen to manage much of their production themselves. This enables them to see further down the supply chain, and they largely work with suppliers at a component or raw

material level. SCA, one of the world's largest companies in personal care products, has its own production sites and it has chosen to place these near its suppliers for a number of different reasons. SCA actively works to involve the workers' representatives at its suppliers. The Volvo Group in fact manages these parts of production itself and is therefore located in close geographical proximity to its suppliers. It is taking a long-term approach to working with its suppliers on sustainability questions, and suppliers are also very much involved in the company's product development process. The retail companies featured in the report also state that geographical proximity and close cooperation with suppliers greatly improves their understanding of a supplier's situation,



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and they all see this as a success factor for increased sustainability.

Many companies engage in efforts with their suppliers to increase knowledge in a number of areas. Investing in supplier training helps to legitimise sustainability questions and it can be a way of establishing long-term relationships with suppliers. Efforts can even be made in areas that help create the structures and processes that prevent violations of human rights in the workplace. For example, this may include training efforts for suppliers at management level to develop and improve routines and processes to meet the sustainability demands placed on them, so-called Management System (MS) training. Worker representation training at the factory worker level is another area that companies and interested parties emphasise as being important.

Cost estimation and planning

The report shows that traditional purchasing practices that primarily focus on pressing prices and shortening lead times run a greater risk of having a negative impact on working conditions. Aggressive cost-orientated purchasing practices risk leading to price pressure, something that interested parties and researchers confirm contributes to extremely low wages and unreasonable levels of overtime. Reverse e-auctions and extended payment terms are two methods that are highly likely to have a negative impact on a supplier's financial stability.

Companies wishing to pursue sustainable purchasing can make a number of changes to prevent their own purchasing behaviours from undermining the ability of suppliers to meet sustainability demands. For example, companies can map

out costs and make estimations that do not focus on cost reduction, for their own part and with the supplier. To avoid a situation in which workers end up being paid a wage that they cannot live on, companies can also estimate the actual costs of production, and then oversee labour costs in proportion to their other production costs. The Swedish clothes retailers Lindex and Filippa K both consider it to be a problem that wages are generally too low and they therefore prioritise remuneration in their sustainability work. Both are planning to use relatively simple cost estimation tools in different ways to plan the levels of remuneration in proportion to other production costs. In addition to this, Filippa K is also placing demands on suppliers to pay a living wage.



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Working on different levels to improve the planning of the production process even more, and doing so in agreement with the suppliers, can help to avoid short lead times and may thereby reduce the risk of short-term contracts, unreasonable and/or mandatory overtime, as well as suppliers using subcontractors. Trend-sensitive products run a greater risk of causing unexpected problems since production often involves short lead times. Companies can benefit from placing orders for trend-sensitive product with their key suppliers, with whom they have good communication and who they know have well-established routines for planning, cost estimation and workers' complaints mechanisms. Several of the companies discussed in the report use different methods to avoid excessive production peaks. Filippa K, for example, systematically tries to schedule the production of its basic collection, Wardrobe Essentials, during low season. Whilst this creates greater security and opportunities for long-term planning for its suppliers, it also means that Filippa K is able to take advantage of favourable prices.

Recommendations

There is a complex situation facing companies that choose to make purchases from low-wage countries. Many factors need to be weighed in and it places a heavy responsibility on the buyer company. Nonetheless, the report shows that several Swedish companies are engaged in working pro-actively to link sustainability and purchasing practices. Purchasing processes can vary greatly from company to company, depending on its organisational structure and on where the different purchases have been made.

FAIR TRADE CENTER GIVES THE FOLLOWING RECOMMENDATIONS FOR DEVELOPING SUSTAINABLE PURCHASING PRACTICES:

- Do not use aggressive cost-orientated purchasing practices
- Prioritise sustainability questions at management level and work actively towards integrating sustainability work with purchasing practices
- There must be a clear workers' perspective in the audit system
- Reward suppliers who work progressively with sustainability questions
- Develop strategic sustainability work based on the type of supplier relationship
- Invest in training to develop skills and knowledge
- Cooperate with local actors on questions concerning co-determination
- Weigh in the supplier perspective when planning purchases
- Analyse levels of remuneration and demand living wages

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